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EX PARTE OR LATE FILED

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Mr. William Caton
Acting Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

**Re: EX PARTE -- Application by Verizon New England for
Authorization to Provide In-Region, InterLATA Services in
Vermont, CC Docket No. 02-7**

Dear Mr. Caton:

Enclosed is an ex parte letter to be filed in the above docket, which has been redacted and is for public inspection. The confidential version of this ex parte letter is being submitted with an appropriate cover letter with the understanding that the confidential material will be fully protected by the Protective Order established specifically for this docket (CC Docket No. 02-7; rel. January 17, 2002) and that the requirements for review and use of this document will be fully satisfied.

Sincerely,



Lori Wright
Associate Counsel
Federal Advocacy

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**Re: EX PARTE -- Application by Verizon New England for
Authorization to Provide In-Region, InterLATA Services in
Vermont, CC Docket No. 02-7**

Dear Mr. Caton:

On February 26, 2002, three days before reply comments were due in the above-referenced docket, Verizon submitted on the record a CD-ROM containing a confidential cost study attempting to defend its UNE rates in Vermont. WorldCom received a copy only one day before reply comments were due. WorldCom stated in its reply comments that due to time limitations we would not be able to fully assess the cost study in our reply comments, but would provide a more detailed response to the cost study in an upcoming ex parte letter. Below we describe our observations and conclusions based on our review of the cost study, in which correcting two errors would lower switching rates by approximately one-third.

AVAILABILITY OF STUDIES

First of all, Verizon's submission contained no working cost models. Rather, Verizon provides only Acrobat (PDF) files containing print-outs of the reports generated by its models, as well as testimony filed by Verizon in the Vermont cost proceeding that

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discusses the cost models. For the models that determine investment levels, the print-outs do not provide the equations and algorithms that the models use, and thus do not permit third parties to adequately assess the effect of alternative inputs. Verizon should provide working cost models in the Vermont proceeding as other BOCs have done elsewhere, e.g., BellSouth in its Georgia/Louisiana section 271 application.

The CD-ROM filed by Verizon does contain, however, both a description of, and the results from, the algorithms that Verizon used in spreadsheets to convert the results of its investment models into monthly costs. Based on these descriptions, third parties are able manually to recreate the computation of monthly costs derived from investments and vary assumptions about some of the inputs, such as the switch installation factor and the use of only business days for setting rates.

SWITCH INSTALLATION FACTOR

Verizon's description of the algorithms confirms that Verizon uses a switch installation factor of ** **, i.e., installation costs are ** ** percent of the material cost of the switch. The factor is computed as the ratio of installed investment to material investment for digital switches, based on data in Verizon's 1995 Continuing Property Records.¹ This factor is greatly overstated and leads to port and usage rates that are overstated. As AT&T noted in its comments in this proceeding, the factor exceeds even the excessive installation factors used by Verizon in both New York and Massachusetts, which were 43.26 percent and 40.27 percent, respectively.

¹ See Workpaper Part B, page 74 of 92, in the file Compliance/04-04-00 Compliance Recurring/Attachments.pdf. A comparison of the total switching investment from these data with the ARMIS data for Vermont filed by Verizon indicates that the digital switch investment data Verizon uses is its entire embedded base, rather than only for switch installations in a single year.

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Verizon's switch installation factor also exceeds the factors used in the Open Network Architecture ("ONA") proceedings in 1992.² In the investigation into ONA rates, SBC provided installation factors for its digital switches that varied slightly from state to state, but included about 10 percent for its own installation costs, and about 15 percent for vendor installation costs.³ These ONA data are presented in the Appendix attached hereto. There is no credible reason why Verizon's switch installation factors should be so much higher than those presented in the ONA investigation.

Based on these ONA data, Vermont's installation factor, including both the vendor installation costs and the Bell company installation costs should fall between 21.2 and 28.8 percent. Even assuming that Verizon's materials costs do not include any vendor installation – and Verizon has not demonstrated that to be the case – the installation factor used in Vermont, and thus the switch usage and port rates, are overstated by between ** ** and ** ** percentage points. Thus, the switch usage and port rates should be cut by between ** ** and ** ** percent.

APPLYING SWITCH COST TO DAYS IN THE YEAR

In addition, the information filed by Verizon on the CD-ROM also confirms that Verizon has excluded all minutes of use on weekends in its computation of switch usage rates. Verizon converts busy-hour minutes to total minutes through the use of a conversion factor that reflects only weekdays.⁴ While it may be the case that usage on weekends and holidays is lower than on weekdays, it is completely unreasonable to claim

² See Declaration of Catherine E. Pitts, AT&T Comments, CC Docket No. 02-7, at page 11.

³ See Direct Case of SBC, CC Docket No. 92-91, May 18, 1992, at Appendix A Figure 1, pages 1-5. Verizon (then NYNEX Telephone Companies) did not file comparable data. However, it is reasonable to assume that the installation costs would not differ markedly among Bell companies. In any case, TELRIC costs should reflect a least-cost, most efficient company. Verizon should not be allowed to use a higher factor than was achieved by another Bell company, absent a strong justification, which Verizon has not provided in this instance.

⁴ See Workpaper B, page 75 of 92.

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that there is no usage at all on weekends and holidays, as Verizon's methodology implicitly does. Ignoring weekend and holiday usage violates the TELRIC principle that all rates (in this case, the rates that CLECs pay for weekend and holiday usage of leased switches) must reflect costs (which, as we discuss below, Verizon is fully compensated for without consideration of this weekend and holiday usage). Here, adjusting the conversion factor to reflect the conservative assumption that usage on weekend days and holidays is half the level of usage on business days – an assumption adopted by the New York Public Service Commission in its recent UNE rate decision – would lower switch usage rates by ** ** percent. Of course, if average daily usage on weekends was more than half the daily usage during the week, rates should be cut even more.

Verizon claims that using any number of days greater than ** ** to estimate annual usage would be inappropriate.⁵ As Verizon explains it, the switch is sized based on busy-hour minutes. These minutes were recorded “in the busiest hour of a business day during a ‘busy’ month.”⁶ Verizon then computes a busy-hour-to-day ratio that “represents the proportion of that day’s traffic that is accounted for by the busy hour.”⁷ Finally, Verizon divides this ratio by a “given number of days” to determine the ratio of busy hour to annual usage.⁸ Verizon justifies using less than all 365 days of the year because “the busy hour represents the *busiest* hour of a *business* day during a particularly *busy* month.”⁹ Evidently, what Verizon means is that since it is measuring usage on a particularly busy hour of a busy day of a busy month, and averaging that usage over all

⁵ See McCarren/Garzillo/Anglin Reply Declaration, Verizon Reply, at ¶ 33.

⁶ *Id.* at ¶ 32.

⁷ *Id.*

⁸ *Id.*

⁹ *Id.* at ¶ 33.

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hours of all business days of all months, the resultant average number is so high that it is fair to ignore weekend and holiday usage altogether.

If this is what Verizon is actually doing, it is fairly criticized as entirely arbitrary, because there is no way to know if the overcounting that Verizon claims is at all equal to the undercounting that Verizon acknowledges. Furthermore, Verizon need not engage in such “rough justice” – it could easily do studies to justify these assumptions, but apparently has not done so.

But as we show in what follows, the more significant point is that Verizon blatantly mischaracterizes its methodology. It does *not* rely on an overly high number of minutes of weekday usage, and therefore nothing in its calculation could possibly warrant ignoring weekend and holiday usage. First, while Verizon does, as it says, *start* with usage on a day’s busy hour, it adjusts for that busy-hour usage so that the daily usage it relies upon actually represents *average* usage on a weekday, *not* busy-hour usage generalized over a full day. Second, Verizon’s claim that it uses a particularly busy day as its sample is pure hyperbole – it uses simply a typical weekday. Finally, Verizon’s claim that it uses a particularly busy month is another misrepresentation – the conversion ratio that Verizon uses corrects for any abnormally high or low usage in that month. Consequently, when Verizon calculates average annual usage during business days, the number it derives represents just that – the actual expected usage of the switch over a year’s business days. As a result, there are no “extra” business day minutes that might somehow justify ignoring the fact that Verizon continues to charge CLECs for the minutes its customers use on the weekends and holidays.

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The ratios Verizon computes are provided in Workpaper Part B, Page 75 of 92. That workpaper shows that Verizon's ratio of busy-hour minutes to all-hours-of-the-day minutes is computed from a traffic sample taken on one day.¹⁰ Thus, applying that ratio to the busy-hour minutes from a business day will convert busy-hour minutes to total minutes for the day containing the busy hour. Because Verizon applies this ratio to the busy-hour figures it starts with, the daily figures it relies upon represent average use over a day, not busy-hour usage. Additionally, there is nothing in the workpapers that demonstrates that the day Verizon used as a sample was a particularly busy weekday. Verizon then converts that amount of minutes to a monthly amount by multiplying this estimate of total minutes for the day containing the busy hour by the ** ** business days in the month – again, no adjustment is made to take into account weekend days.¹¹ . Finally, Verizon calculates an annual number of minutes by multiplying the result of the previous calculation by the ratio of ** ** traffic to annual traffic, based on a traffic study it performed. This ratio is ** **, i.e., minutes in ** ** represent ** ** of the minutes in a year.¹² And, as with the ratio of busy-hour minutes, since the ratio is based on a traffic study designed to assure that ** ** minutes are properly adjusted on an annualized basis, if ** ** were a particular busy month the ratio would have corrected for this fact and ensured that the annualized figure represented average annual usage, not

¹⁰ Further confirmation that this ratio was taken based on traffic on a single day, is Verizon's description of the ratio as "the proportion of that days traffic that is accounted for by the busy hour." [Emphasis added] *Id.* at ¶ 32.

¹¹ Verizon states that the basis for using ** ** was the calendar. The month of ** ** that Verizon used for its traffic study had 31 calendar days, and contained ** ** weekends of two days each, yielding the ** ** business days Verizon uses. Thus, no adjustment was included in this count of days to reflect any weekend usage.

¹² Since ** ** is ** **, or ** ** percent of the months in a year, it is hard to see how ** ** can be truly characterized as "a particularly *busy* month." Indeed, since ** ** is ** **, or ** ** percent of the days in a year, having only ** ** percent of the minutes in the year would imply that ** ** is a slightly *less* busy month than average.

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usage based on a particularly busy month. In any event, since the traffic study produced a ** ** ratio, and since there are 12 months in the year, it appears that ** ** is not in fact a particularly busy month at all, but an absolutely average month.

In sum, the workpapers make clear that the annual figure over which Verizon spreads all of its usage-sensitive switching costs represents average annual workday usage, not usage typical of a busy hour on a busy day on a busy month. Moreover, at no step in this chain used by Verizon to expand busy-hour minutes to annual minutes does Verizon account for any usage on the weekends.¹³ As a result, the charges Verizon assesses over the year's weekdays fully compensate Verizon for all of what it claims are its usage-sensitive switch costs. It necessarily follows that all usage-sensitive switching charges assessed CLECs for their customers' weekend and holiday calls are pure gravy for Verizon – all of its alleged costs have been fully recovered in charges for weekday usage. This is a fundamental TELRIC error that grossly distorts the switching rates.

Furthermore, SCIS includes an input for the ratio of peak to average busy-hour minutes.¹⁴ It is this peak number of minutes that SCIS uses to size the switch. If Verizon has truly picked a business day for its traffic study that is busier than the average business day, then this ratio needs to be adjusted downward to reflect that fact. Otherwise, the busy hour investment produced by SCIS will be inflated, as well as the monthly switch costs developed from that investment.

Verizon cannot have it both ways. Either it should derive busy hour minutes of use from its annual minutes by applying its conversion factors, or it should start from (an

¹³ Verizon apparently has a traffic study that looks only at weekday usage, but it declines to publish its results or rely on in its calculation of charges.

¹⁴ Verizon has selected inputs for this ratio of ** ** in the urban zone and ** ** in the suburban and rural zones. See Workpaper Part B, page 77 through 80 of 92.

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estimate of) busy-hour minutes and build that up to an annual number of minutes. The first method would assure that the switch is not oversized for the actual annual demand, while the second would assure that the annual demand used to compute the per minute rate would be consistent with the demand used to determine the switching investment. In both cases, weekend minutes must be included.

In sum, Verizon must include weekend use in its computation of switch rates for a reduction of switch usage rates of at least ** ** percent, and should make reductions for the overstated switch installation factors, which would account for an additional reduction of at least ** ** percent, as described above. This would result in a total reduction in switching costs of at least ** ** percent. Depending on the installation factor used, the rates for local switching would be either ** ** or ** ** for usage, and ** ** or ** ** for port, after these two changes are made.

DOUBLE CHARGING FOR INTRASWITCH CALLS

Verizon proposes to charge both an originating and terminating charge for intra-switch calls, i.e., calls between two customers served by the same switch. Verizon, which has the burden of proof on this matter, claims this is justified because “every call involves the same ‘originating’ and ‘terminating’ switching activities...irrespective of how many switches are involved.”¹⁵ This assumption is incorrect. For an intra-switch call, the switch receives the dialed digits, determines that the called number is served by it, and routes the call to the called line. For an inter-switch call, the switch receives the dialed digits, determines that the called line is not served by it, determines through the SS7 network where to route the call, opens a trunk to the terminating switch and passes the call through. The terminating switch then receives the call, determines which line is

¹⁵ See McCarren/Garzillo/Anglin Reply Declaration at ¶ 36.

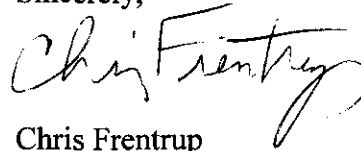
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the called party, and passes the call through to that line. Thus, an inter-switch call is processed two times by two separate switches, while an intra-switch call is processed only once by one switch. Verizon fails to charge less for intra-switch calls based on its claim that intra-switch calls and inter-switch calls generate identical costs. Since this is not so, and since Verizon's costing of intra-switch calls is otherwise unsupported it plainly fails to meet its burden of showing that its rates are cost-based.

Because Verizon's switching rates are inflated for the reasons described above, Verizon's section 271 application for Vermont should be denied.

Please do not hesitate to contact us if you would like to discuss this matter further.

Sincerely,

A handwritten signature in black ink that reads "Chris Frentrup". The signature is written in a cursive, flowing style with a large, sweeping "C" and a long, trailing flourish at the end.

Chris Frentrup

APPENDIX

		Source ¹	AR	KS	MO	OK	TX
Ratio of Material to Material + Vendor EF&I	A	Appendix A, Figure 1, Line 2, page 1-5	0.851600	0.834000	0.857000	0.902800	0.829400
Sales Tax Factor	B	Appendix A, Figure 1, Line 3, page 1-5	0.044100	0.047100	0.045299	0.061899	0.075299
Vendor EF&I	C	$(1 - A) / [A * (1 + B)]$	16.7%	19.0%	16.0%	10.1%	19.1%
TELCO Engineering	D	Appendix A, Figure 1, Line 5, page 1-5	0.050819	0.048450	0.029312	0.036757	0.027308
TELCO Plant Labor	E	Appendix A, Figure 1, Line 6, page 1-5	0.028390	0.049744	0.059255	0.073372	0.036827
TELCO EF&I	F	D + E	7.9%	9.8%	8.9%	11.0%	6.4%
Total EF&I	G	B + F	24.6%	28.8%	24.8%	21.2%	25.5%

1 All sources are from Direct Case of Southwestern Bell Telephone Company, CC Docket No. 92-91, filed May 18, 1992